

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

In the Matter of)	
)	
Integrated Resource Planning for the)	PSC Docket No. 06-241
Provision of Standard Offer Supply Service)	
By Delmarva Power & Light Company)	
Under 26 <i>Del. C.</i> § 1007(c) & (d): Review)	
And Approval of the Request for Proposals)	
For the Construction of New Generation)	
Resources Under 26 <i>Del. C.</i> § 1007(d))	
(Opened July 25, 2006))	

**COMMENTS OF
CONSTELLATION ENERGY COMMODITIES GROUP, INC. AND
CONSTELLATION NEWENERGY, INC.
ON THE DELAWARE PUBLIC SERVICE COMMISSION STAFF REPORT**

I. INTRODUCTION

Pursuant to Order No. 7287, issued by the Delaware Public Service Commission (“Commission” or “PSC”) on September 18, 2007 in the above-docketed proceeding,¹ Constellation Energy Commodities Group, Inc. (“CCG”) and Constellation NewEnergy, Inc. (“CNE”) (collectively, “Constellation”) hereby submit these comments regarding the *PSC Staff Report on the Term Sheets for Proposed Power Sales to Delmarva Power*.² Constellation herein responds to the Commission Staff’s evaluation of potential pricing under Bluewater Wind Delaware, LLC’s (“Bluewater”) Term Sheet originally filed on September 14, 2007 and, more generally, assesses the need at this time to require Delmarva Power & Light Company (“Delmarva”) to enter into any form of long-term power purchase agreement

¹ See Order No. 7287, Commission Docket No. 06-241 (issued Sept. 18, 2007).

² See *PSC Staff Report on the Term Sheets for Proposed Power Sales to Delmarva Power*, Commission Docket No. 06-241 (submitted Oct. 29, 2007) (“PSC Staff Report”).

(“PPA”) with Bluewater in order to promote investment in new resources to serve Delaware’s consumers. Constellation also addresses in these comments Commission Staff’s calls for a “portfolio approach to energy planning.”³

II. BACKGROUND ON CONSTELLATION

CCG is a power marketer authorized by the Federal Energy Regulatory Commission (“FERC”) to sell energy and capacity and certain ancillary services at market-based rates.⁴ CCG focuses on serving the full requirements power needs of distribution utilities, co-ops and municipalities that competitively source their load requirements. CCG also sells natural gas and other commodities at wholesale, both in the U.S. and abroad, and holds interests in exploration and production companies. CCG does not own any physical assets for the generation, transmission or distribution of electric power and has no retail electric customers or service territories. However, CCG bids energy, capacity and ancillary services into the PJM Interconnection, L.L.C. (“PJM”) administered markets on behalf of generation-owning affiliates.

CNE is a leading national competitive retail energy supplier to commercial and industrial customers, serving more than 10,000 customers in 17 states and two Canadian provinces. These 10,000 customers represent approximately 15,500 megawatts of demand. CNE is committed to providing customized energy-related products and services to customers in the competitive electricity marketplace.

Since the introduction of customer choice in Delaware’s electric industry, CNE has been an active participant in the Delaware retail market. CNE provides service to commercial

³ PSC Staff Report at p.5.

⁴ See *Constellation Power Source, Inc.*, 79 FERC ¶ 61,167 (1997) (FERC order initially granting CCG market-based rate authority).

and industrial customers in Delmarva's service territory, as well as in various service territories throughout PJM.

CNE and CCG are active in wholesale and retail markets nationwide. Moreover, CNE and CCG have been active in virtually all of the regulatory proceedings before the Commission involving the provision of standard offer service ("SOS") to Delaware's customers and have served as advocates for fair and competitive open markets that are designed to provide customers with an array of competitive options. As such, Constellation is well positioned to assist the State Agencies in examining means to facilitate the entry of new resources into Delaware's electric infrastructure.

III. COMMENTS

A. The State Agencies Should Heed the Recommendations of the PSC Staff Report and Deny Bluewater's and Others' Long-Term Generation Proposals.

Constellation agrees with Staff's assessment that any long-term generation proposal to serve SOS "is – at this time – not in the public interest and is not consistent with the underlying principles of the Electric Utility Retail Customer Supply Act of 2006 ('EURCSA'),"⁵ which requires that any long-term generation proposal must "achieve the greatest long-term system benefits in the most cost-effective manner"⁶ In summarizing its reasons for recommending rejection of the long-term generation proposal, Staff states, *interalia*, that the project is not in the public interest because: (1) it includes "a commercially unreasonable pricing escalator [and] imposes significant additional risk as well as cost on Delmarva's SOS ratepayers"; (2) "Bluewater shifts the project's risk associated with cost increases during construction to Delmarva SOS ratepayers, and thus, the ratepayers – *not*

⁵ PSC Staff Report at p.4.

⁶ PSC Staff Report at p.4.

Bluewater – assume full responsibility for any losses incurred with the project delay and/or failure”; (3) “delayed timing of the revised project results in additional cost and exacerbates the price risk”; and (4) “negotiations resulted in a more expensive, less favorable project than the original bid proposal”⁷

In response to the PSC Staff Report, Bluewater submitted a filing in which it “proposes to . . . eliminate [the] escalators entirely.”⁸ Bluewater believes that its “proposal resolves many of the concerns expressed in the Staff Report and . . . requests [that] the State Agencies allow Bluewater the opportunity to discuss this proposal and/or resolve any other remaining issues with PSC Staff and the [Independent Consultant].”⁹

Constellation urges the State Agencies to uphold the Staff’s recommendation and deny Bluewater’s request, as it fails to address *many* of the concerns in the PSC Staff Report, and as it may fail to result in “a more diverse supply at the lowest *reasonable* cost,”¹⁰ as required by the EURCSA. Not only has Bluewater failed to adequately address Staff’s concerns with respect to “uncertainty with regard to project viability,” but saddling Delaware’s consumers with the costs of a long-term PPA entered into by Delmarva for wind generation may not represent a *reasonable* cost. Constellation submits that any need for long-term PPAs for Delmarva is vastly overstated. In the past, the emerging merchant power industry relied heavily upon traditional debt financing of 80 to 100 percent that was supported by long-term PPAs with utility customers. Today, however, other sources of capital are pouring into energy infrastructure. Balance sheet equity, hedge funds and private equity firms are all

⁷ PSC Staff Report at p.4.

⁸ *Bluewater Wind Delaware LLC’s Submission in Response to PSC Staff October 29, 2007 Report on the Term Sheets for Proposed Power Sales to Delmarva Power*, Commission Docket No. 06-241 (submitted Nov. 6, 2007) (“Bluewater Nov. 6 Response”) at pp.24-25.

⁹ Bluewater Nov. 6 Response at p.26.

¹⁰ 26 *Del. C.* § 1007(c)(1)(b) (*emphasis added*).

coming forward to invest in and acquire new renewable generating resources, traditional fossil generating resources and demand reduction technologies. The recent implementation of forward capacity markets in several regions, including PJM, has further added to the interest of these investors and is further increasing the amount of capital available. The Texas market provides proof of this, where its market has witnessed a major construction boom in new generation capacity – including gas, oil, coal, and wind – all without long-term rate base PPAs. In addition, companies like Constellation are in some cases entering into long-term bilateral purchase agreements with renewable and traditional fossil-fuel generators in order to supply either retail or wholesale customers, without the need for a traditional rate base from which to recover the cost of those purchases. For instance, Constellation has or will purchase renewable power from:

- Reddington Mountain Wind (Maine) – 90 MW (100% of output) of wind energy, capacity and renewable energy certificates (“RECs”) under a 10-year agreement;
- Brightfields/City of Brockton (Massachusetts) – 400 kW of solar energy, capacity and RECs under a 20-year agreement; and
- Equinox (Vermont) – RECs under a five-year purchase agreement from a facility which has not yet been permitted.

Moreover, within the PJM footprint in which Delaware resides, CNE entered into a 10-year, 30 MW power purchase agreement for wind power from an Edison Mission Group wind resource in Somerset County, Pennsylvania.

At the same time as private entities are making such investments, the costs which result from long-term PPAs are becoming more apparent. The stranded costs which arose from implementation of the Public Utility Regulatory Policies Act (“PURPA”), for instance,

have revealed the risk to rate base customers of being locked into paying for long-term investment decisions which are made on their behalf by regulators and utilities. In addition, rating agencies such as Standard & Poor's are now treating long-term PPAs as imputed debt obligations of the purchasing utility, reflecting the view that it is the utility and its customers who bear all of the investment risk under such long-term PPAs.

Because the need is overstated and because the costs are becoming increasingly apparent as the industry evolves, Constellation urges the State Agencies to approve the use of long-term contracts only very sparingly, if at all. The EURCSA grants Delmarva the *ability* to consider and enter into such PPAs, but does not *require* their use; it allows the use of long-term PPAs only for projects that provide “more diverse supply at the lowest reasonable cost”¹¹ and “that result in the greatest long-term system benefits”¹²

With respect to nearly all renewable and traditional fossil based resources, *siting* rather than financing is the major impediment to new investment. This is not to say that there are not perhaps some resources whose development may require some form of long-term commitment. The only example of such a resource which we are convinced presently may require such long-term commitment is investment in nuclear power. Nuclear plants require a very long lead time for development, with significant capital costs, as well as a very long time period over which capital outlays must be recovered. Assuring safe and secure operations, proper handling of nuclear material, adequate funding of future decommissioning and investment in twenty-first century nuclear generation technology all make these investments unique and require greater financial stability and continuity of ownership than investment in any other type of generation resource. For these reasons, Constellation supports the use of

¹¹ 26 Del. C. § 1007(c)(1)(b).

¹² 26 Del. C. § 1007(d)(3).

long-term contracts, if any, only to support unique resources such as nuclear generation as part of a policy of fuel diversity and to address the compelling problem of global climate change.

B. Delaware Should Rely Mainly on a Portfolio of Resources Obtained Through the Existing SOS Request for Proposals (“RFP”) Process.

In the PSC Staff Report, in addition to denying the bids for PPAs with new generation, Staff calls for the State Agencies to:

adopt a portfolio approach to energy planning that would involve the addition of new generation assets in southern Delaware, development of DSM and energy efficiency programs, renewable distributed generation, short- and long-term bilateral contracts, and market purchases.¹³

Constellation urges the Commission to reject any proposal to require Delmarva to *actively* manage a portfolio of resources, and instead asks the Commission to continue its support of the current structure in which Delmarva is relieved from this type of responsibility and procures a portfolio of full requirements resources through a competitive RFP process. The current SOS RFP structure already provides a proper balance between obtaining the most competitive prices for consumers and maintaining a reasonable level of price stability from year-to-year. Moreover, requiring Delmarva to not only hold RFPs for meeting their SOS load requirements, but also to retain personnel or hire outside consultants and expend resources to actively manage an energy portfolio by additionally making other shorter and longer term purchases and acquiring and managing generation is an inefficient way to achieve competitive SOS prices for consumers. As Delmarva’s load must always be met with full requirements products, in order to actively manage its load obligations, Delmarva (or its consultants) would have to retain individual experts who understand and follow not only

¹³ PSC Staff Report at p.7.

electric energy and other commodity markets, but also ancillary services, capacity and renewable products markets.

The Delmarva SOS RFPs have resulted in prices that are reflective of the market, but insulate customers from the volatility of any one given procurement period through a structure which bids out only one-third of Delmarva's smaller customer SOS load for three-year periods at each procurement cycle. Constellation believes that the Commission has established a rational and balanced approach by allowing rolling three year contract terms for averaging prices and a three year contract term for wholesale SOS supply for smaller customers. Over a three year period, suppliers have access to a wide variety of market products and time periods with which to serve the SOS load. They have the flexibility to hedge load over time in various near-term and long-term markets. By allowing the supplier to respond to market signals over a three year period of time, the supplier has flexibility with which to procure its supply. This in turn allows the supplier to offer more competitively priced products. Moreover, the carefully structured SOS supply procurement process using "laddered" three-year contracts best serves to mitigate the impacts of price fluctuations in market prices from year to year.

Constellation believes that wholesale suppliers – rather than independent consultants or utilities themselves – provide the most cost-effective method of SOS supply management for utility load. Wholesale suppliers are experts in the area of portfolio management, and have greater resources, expertise and ability to appropriately manage portfolios of supply at the least possible cost. These wholesale suppliers pass on the savings they achieve due to their sophisticated risk management skills in the form of more competitive bids for full requirements SOS products in the SOS RFPs. Wholesale suppliers have already invested in,

and continue to make significant investment in acquiring, experts in each specific type of market which make up full requirements SOS supply. These experts understand and are able to best analyze and make purchases for the lowest costs for each type of product. These experts use far more than the electric markets and reliance on bilateral contracts for physical supply in order to manage their price risk position – *e.g.*, they utilize gas, coal and nuclear fuel markets, futures, swaps and derivative products and other hedging instruments.

In summary, it is best to allocate to wholesale suppliers – rather than Delmarva and, in turn, Delmarva’s consumers – the risks and responsibilities associated with active portfolio management. Wholesale suppliers who submit bids in the SOS RFPs are in the best position and are best equipped to bear such risks and responsibilities.

III. CONCLUSION

The EURCSA outlines that “[a]t least 30 percent of the resource mix of [Delmarva] shall be purchases made through the regional wholesale market via a bid procurement or auction process held by [Delmarva].”¹⁴ In the absence of new generation projects which provide the lowest reasonable cost and provide long-term system benefits, the State Agencies, for the reasons stated herein, should promote use of the existing SOS RFP process to meet Delmarva’s SOS load requirements. Constellation appreciates this opportunity to submit its comments and is convinced that rejection of the long-term generation proposals, along with maintenance of Delaware’s existing SOS RFP process will ensure that Delaware’s consumers will receive competitive SOS prices through a fair, transparent and robust competitive procurement process.

¹⁴ 26 Del. C. § 1007(c)(1)(a).

Respectfully Submitted,

/s/

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On Behalf of
Constellation Energy Commodities Group, Inc.
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November 13, 2007

CERTIFICATE OF SERVICE

PSC Docket No. 06-241

I hereby certify that I have this day served by email and first class mail (and by express mail to the Commission), Constellation's Comments in the above-referenced proceeding upon each person designated on the official service list in these proceedings.

Dated at Baltimore, MD this 13th day of November, 2007.

/s/

Divesh Gupta